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SUBJECT: MADRID WEEKLY ECON/AG/COMMERCIAL UPDATE REPORT -
MAY 21

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EINV: All time high for Spanish stock market
EINV/ETRD: Decline of the real estate market
EAGR/ETRD: US beef and EUR market
EINV/ECON: US owned Texas Pacific Group teams up to buy Iberia
EINV: Iberdrola to sell 20% for quick cash
EINV/ETRD: Tourism up in Spain
ELAB/EFIN: Degree or no degree - pay gap decreases
SENV: Is the drought finally over?

SPANISH STOCKMARKET IBEX-35 HITS ALL-TIME HIGH

11. (U) Shaking off (at least for now) jitters of a few weeks ago, the IBEX-35 hit an all-time high on May 23 of 15,229.9 points. The market is up 7.62% so far this year. Despite fears of a housing market slowdown, even the big construction firms such as Ferrovial, ACS, FCC, Sacyr and Acciona have run up stock gains. There may even be room for more gains. Merrill Lynch, for instance, says Ferrovial's stock is worth 24% more than it is currently traded. Continued strong Spanish economic growth during the first quarter of 2007 (4.1% on an annualized basis) no doubt helps underpin the stockmarket. In addition, the Spanish Institute of Statistics (INE) published numbers on May 23 indicating that industry and investment are becoming relatively more important than construction and personal consumption as growth drivers. Even productivity is up somewhat. However, all analysts agree Spain still remains vulnerable to construction slowdown induced lower growth, or even a recession at some point. (Comment: The INE numbers are especially important as the government argues that it is changing Spain's growth model. El Pais, considered close to the government, comments in its May 24 editorial that there are some signs the government's economic policies are having an effect, although Spain still remains dangerously over-reliant on construction. The newspaper adds that it will take several years to reduce this reliance and skillful management of the economy to avoid a "hard landing.") (Expansion, May 24, 2007; El Pais, May 24, 2007)

DISINFLATION OF THE REAL ESTATE MARKET

12. (U) New data reaffirms the slow but sustained descent of the Madrid real estate market. The Spanish Mortgage Association figures show that in 2006, 68.9% of a family's income went into the purchase of a new home, 3 points less than the previous year. While a Morgan Stanley study has dramatically decreased the consequences of increase of the types of interest of mortgages to Spanish families. Those who closed before 2003, a supposed 82%, contracted interest rates at a similar or higher than the current rate. Concluding that only 18% of families would be seriously

affected by the unstoppable increase of the Euribor in the last three years. (20 minutos, May 22)

US BEEF MAD COW FREE

¶3. (U) On May 22, 2007, at the annual meeting in Paris of the World Organization for Animal Health (OIE), the United States was recognized as having a controlled risk status for BSE (mad cow's disease). This decision is important, because it opens the door for the U.S. Government to request that countries, which had closed their borders to U.S. meat exports because of BSE, reopen their markets. Korea is a prime example and target.

¶4. (U) While there is some discussion of making a special effort to present this new international recognition to the European Commission (EC), with the opportunity of presenting it to the individual Member States, U.S. meat-access problems in Europe stem from the EC's unwillingness to open European borders to U.S. beef produced using synthetic hormones. The EC lost a WTO case on this issue, but has not relented, providing U.S. beef exporters a small, overly-managed quota for non-hormone-treated beef. In addition, the U.S. Government applied tariff retaliation on specified European exports to the United States.

¶4. (U) The U.S. Government is talking to the EC about the possibility of providing U.S. beef exporters additional access for non-hormone-treated beef. However, there are additional market-access problems associated with EC certification of U.S. meat packing plants, the use of anti-microbial treatments on carcasses, not to mention that the requested increase in the quota and the counter-offer are light-years apart, all of which will likely slow or impede near-term success on this front.

AIRLINE PURCHASING WARS

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¶5. (U) Texas Pacific Group (TPG) teams up with British Airways (BA) and Spanish companies Vista Capital, Ibersuizas, and Quercus to buy Iberia: Should the takeover bid succeed, Spanish firms would retain a majority of the voting rights. This is necessary for Iberia to maintain lucrative routes to Latin America. Santander is involved in financing the takeover bid. The American firm is known for having previously purchased Continental Airlines and recently bought Alltel together with Goldman Sachs. (Comment: Interestingly, the TPG/BA bid has not provoked nationalist reactions, presumably because the majority of the voting rights would remain in Spanish hands. Nonetheless, if this bid prospers on one of Spain's "flagship" companies, it would say a lot about Spanish receptivity to foreign investment.) (Expansion, May 22, 2007)

RENEWABLE ENERGY BUSINESS FOR SALE

¶6. (U) Iberdrola to sell 20% of its renewable energy business and hopes to raise Euros 4 billion on the stockmarket: Iberdrola needs the money given its recent Euros 17.1 billion purchase of Scottish Power. The renewables business is grouped together in the Ibernova subsidiary. Even after the sale Iberdrola will maintain control of Ibernova. Wind power is overwhelmingly what Ibernova does in the renewables area. It already generates a significant share of its business in the U.S., and its largest expansion plans are in the U.S. (El Pais, May 23, 2007)

TOURISM INCREASES IN SPAIN

¶7. (U) In the first quarter of 2007, there was a 2.7% increase in tourism over the previous year. According to a GoS FRONTUR survey a total of 14.9 million tourists came to Spain during the first quarter, primarily to Madrid, Andalucia, and Valencia. The increases were mainly

attributed to tourists from the US, Portugal and Ireland.

DECREASING PAY GAPS FOR THOSE WITH DEGREES

18. (U) The salary difference in Spain for those with degrees and those without is decreasing. According to a recent report by the "Servicio de Estudios de la Caixa" the salary gap between those with university degrees and those with high school degrees fell 40% between 1997 and 2004. The study indicates that the decrease is caused by a saturation of the market of university degrees without a similar increase in corresponding jobs. Ten years ago, 19% of Spaniards between the ages of 25 and 64 had college degrees. In 2004, that rate increased to 26%. This overabundance of workers with degrees has decreased the value of a university degree and forced many to take lower-paying jobs.

RAIN RAIN GO AWAY

19. (U) Unusually high rainfalls over the past few weeks across Spain have caused flooding in various parts of the country, particularly in Castilla-La Mancha, the Mediterranean coast, and Madrid. The rains have affected railways traffic in such cities as Madrid, Valencia, Alicante and Murcia. Well-used road-ways in Madrid such as the M-30 beltway, including a number of newly opened Madrid tunnels have also suffered severe flooding, days before the local elections. Given that Madrid mayoral candidate and incumbent Alberto Ruiz-Gallardon (PP) has toted his accomplishments in public work programs and roadways, it remains to be seen whether the rains will affect the votes. Despite the heavy rainfall, reservoirs have still not reached their full levels, some recent estimates indicating that the reservoirs were only at 64.8% of total capacity. Previous droughts were severe enough that even with the recent abundance of rain, water levels are still below their ten-year average.

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